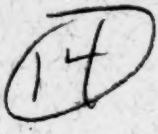

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

No. 770

COOPERATIVE TRANSIT COMPANY,
Petitioner,

vs.

WEST PENN ELECTRIC COMPANY, A CORPORATION, WEST PENN RAILWAYS COMPANY, A CORPORATION, TRI-STATE IMPROVEMENT COMPANY, A CORPORATION, ET AL.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

JAY T. MCCAMIC,
Counsel for Petitioner.

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CITATIONS.

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WEST PENN ELECTRIC COMPANY, A CORPORATION, WEST PENN RAILWAYS COMPANY, A CORPORATION, TRI-STATE IMPROVEMENT COMPANY, A CORPORATION, WEST PENN SYSTEM CONSTRUCTION COMPANY, A CORPORATION, WEST PENN SECURITIES DEPARTMENT, INC., A CORPORATION, CENTRE FOUNDRY & MACHINE COMPANY, A CORPORATION, CLARA NARRIGAN.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

To the Honorable the Supreme Court of the United States:

I.

The petitioner, Cooperative Transit Company, a corporation, organized under the laws of the State of West Vir-

ginia, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Fourth Circuit entered in the above entitled cause on the 2nd day of January, 1943 (R. 73), affirming the order or judgment of the District Court for the Northern District of West Virginia, entered on the 5th day of August, 1942 (R. 63).

Opinions Below.

1. An opinion written by the Hon. Wm. E. Baker, District Judge (R. 57) is reported in 46 F. Supp. 59.

2. An opinion of the Circuit Court of Appeals (R. 66), Hon. Armistead M. Dobie writing, is not yet reported.

Jurisdiction.

The judgment affirming the order or judgment of the District Court for the Northern District of West Virginia was entered by the Circuit Court of Appeals for the Fourth Circuit on the 2nd day of January, 1943 (R. 73). The jurisdiction of this court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. A. 347 (a)).

Questions Presented.

I.

A Traction Company made a mortgage with an after-acquired property clause. It was a subsidiary and affiliated corporation in a group or unity of corporations called "West Penn System". The officials of the System who were also officers of its parent company secretly caused title to an after-acquired car-barn property, bought and paid for by the Traction Company to be transferred to another subsidiary wholly owned, controlled and dominated by the same parent, for the express purpose of preventing the lien

of the Traction Company's mortgage and after-acquired property clause from attaching. The mortgage was foreclosed in a receivership and winding-up proceeding in a Federal District Court and all of the property covered by the lien of the mortgage, both legal and equitable, was sold pursuant to a decree of the court, sale confirmed and deed made with a covenant of further assurances to the purchaser.

No disclosure of the ownership of the car barn by the Traction Company was ever made either to the trustee, the Receiver or the District Court. The trustee in the mortgage, the parent of the Traction Company causing the transfer of title, its holding company, and the subsidiary holding title were parties to the suit. The purchaser upon discovery of the facts, filed an ancillary and supplemental complaint in the same District Court, making party defendants: the trustee in the mortgage, the aforesaid holding company, the parent corporation of the Traction Company and the owned and controlled subsidiary to whom the original transfer was made (all of whom were parties to the prior receivership) and two other owned and controlled corporations in the said System holding title after receivership, and the present holders of title who took with notice and insisted that the purchase money be placed in escrow awaiting determination of ownership.

Whether or not there is ancillary or supplemental jurisdiction in the District Court to construe the decree of sale, to rectify the fraud, to bring in the property or to reach the proceeds of sale?

II.

Whether or not the presence of the two defendants now holding title with notice (whose purchase money is in escrow by their insistence) and who are not bona fide pur-

chasers, but not parties to the original foreclosure suit, destroys the ancillary character of the proceeding of the purchaser?

III.

Whether or not the District Court has yet exhausted its jurisdiction as to the equitable interest of the Traction Company in the car barn property?

IV.

Whether or not the subsidiary and the two defendants holding title can be dismissed if not proper parties, and the suit proceed nevertheless against the parent corporation and subsidiaries originally perpetrating the fraud who were parties to the original foreclosure suit and alternative relief given against them in the form of accounting for the value of the concealed and withheld after-acquired car barn property?

V.

Whether or not the disclosure of the fraud to the Federal District Court conducting the winding-up and foreclosure invests it with ancillary jurisdiction of an inherent nature of a suit by any party to the original foreclosure suit against any of the parties participating in the fraud, to investigate the fraud?

VI.

Whether or not a purchaser at the foreclosure sale of all the property, legal and equitable, coming under the lien of the mortgage, free and clear of all claims including equity of redemption, who has paid the cash consideration, assumed the obligations of the Receiver and payment of all taxes which were liens on the property, can ask for construction of the decree of sale?

Statement.

Wheeling Traction Company operating a street car system in and about Wheeling, West Virginia, had a mortgage made in 1901 with an after-acquired property clause, with no sinking fund provision (R. 4, 5). The Traction Company was insolvent when the mortgage fell due in 1931, and a winding-up and foreclosure suit was begun in the District Court for the Northern District of West Virginia; a receiver was appointed (R. 9, 30). The decree of foreclosure found the mortgage binding and subsisting lien upon all of the property and assets of the Traction Company of every kind and description (R. 7). The property covered by the lien of the mortgage was sold in 1933, the sale confirmed and a Special Master's Deed made to the purchaser (R. 9, 10, 11). The several decrees of foreclosure, of sale, and of confirmation, used the language of the mortgage, and its after-acquired property clause included all the property and assets of the Traction Company covered or embraced in the lien of the mortgage (R. 4-9). The Master's Deed contained like language with a covenant of further assurances (R. 44-51). The sale was free of any right or equity of redemption of the Traction Company, its creditors and stockholders and of all persons claiming under them or against said property (R. 49). The purchaser acquired the equity of redemption.

The Cooperative Transit Company became the purchaser (with an exception not material here) (R. 44). It filed its complaint in the District Court in the nature of an ancillary and supplemental bill, setting out that title to an after-acquired property owned by the Traction Company—a car barn—had been secretly withheld from the Traction Company to prevent the lien of the mortgage and its after-acquired property clause from attaching. The facts had not been disclosed in the foreclosure proceedings (R. 12-25).

The fraud was the following: West Penn Railways Company owned all of the stock of Wheeling Traction. The Traction Company was managed as a department of the "West Penn System" (R. 17). West Penn Railways Company was entirely owned by West Penn Electric Company (R. 14, 15, 16, 17, 18).

The Wheeling Traction Company authorized the purchase of a car barn site in 1916 (R. 18). One was finally purchased in 1919 for $43,200.00 and title taken in the name of Clifford P. Billings, Vice-President and General Manager of the Traction Company (R. 18). West Penn Railways Company paid the $10,000.00 down payment and $3,000.00 agent's commission. Four notes of $8300.00 secured by a deed of trust were given by Billings and wife for the deferred purchase money (R. 18).

Tri-State Improvement Company, a Delaware corporation, wholly owned by West Penn Railways Company, was organized to take title, and took title expressly as "intermediary" for Wheeling Traction Company (R. 19).

On May 19, 1920 the Traction Company reimbursed West Penn Railways Company for its advances of $13,000 with interest (R. 19). The Traction Company was directed to enter a charge on its books against Tri-State Improvement Company (R. 19). The Financial Officer of the West Penn System in directing the charge, advised that "Tri-State Improvement Company is simply acting as intermediary for the Wheeling Company and should receive all necessary funds from that Company." (R. 19). The Traction Company also paid the deferred purchase money (R. 20). In 1923 a car barn was erected at a cost of $50,950.00 and improvements added costing $30,000.00. All this was paid for with Traction Company money (R. 21).

Wheeling Traction occupied the property, paid the taxes and paid no rent for its use (R. 22).

In April, 1924, a financial officer of the West Penn stated:

> "* * * it would be well to allow the Gilchrist property to remain in the name of the Tri-State Improvement Company and to have the Wheeling Traction Company bill the Tri-State Improvement Company for all improvements and extensions actually made on the property for the car barn and other services. I have in mind the approach of the time when the Wheeling bonds become due * * *". (R. 21)

The bonds fell due in 1931 (R. 5).

Up to the year 1924 Wheeling Traction paid dividends and in that year 15½% was declared, amounting to $350,445.00 and payable to West Penn Railways Company as sole stockholder (R. 23). To get funds for such dividends, the West Penn Railways Company loaned the Traction Company $250,000 and took its note (R. 23).

After 1927 the Traction Company had yearly deficits (R. 23).

On May 1, 1928 when the Traction Company was hopelessly insolvent, the total cost of the car barn property $144,767.80 was by order of the West Penn Railways Company, transferred from a book account against Tri-State Improvement Company to the West Penn Railways Company, which proceeded to credit it against the open account the Traction Company owed it (R. 23, 24, 30). After this Traction Company paid Tri-State Improvement Company rent of $1,000 per month until the foreclosure proceedings. The Receiver in those proceedings paid no rent (R. 27).

In 1932 during the foreclosure and wind-up proceedings title was transferred to West Penn System Construction Company, which in 1933 conveyed to West Penn Securities Department, Inc. (R. 13, 14).

Since 1933 Cooperative Transit Company operated the property as a street railway. From 1933 to 1935 Cooperative Transit Company used the car barn without payment

of rent. In 1935 it entered into an agreement with Pan Handle Traction Company (a connecting railway) whereby the latter paid rent for the car barn. From May 1, 1935 to October 31, 1941 the Cooperative Transit Company paid the West Penn Securities Department, Inc. $250.00 per month, rent for the car barn (R. 32, 33).

In 1941 Cooperative Transit Company discovered the above facts under circumstances which are pleaded (R. 27, 28, 29) and learning that West Penn System Securities Department, Inc. was negotiating for sale of a part of the property to defendants, Centre Foundry & Machine Company and the balance to Clara Narrigan, it gave the prospective purchasers immediate and express notice of its interest in the property (R. 29). They nevertheless took a deed for the property, but they required of West Penn Securities Department, Inc. that the purchase money be deposited in escrow until ownership should be determined (R. 29, 30).

Of the West Penn corporation, all save two were parties to the original foreclosure suits (R. 3). Everyone of the West Penn corporations holding title were small corporations of $10,000 authorized capital, wholly owned either by West Penn Railways Company or West Penn Electric Company, which wholly owned West Penn Railways Company. The same group of officers functioned for all these corporations (R. 14, 15, 16, 17, 18)

The complaint categorically charges that title to the car barn property was kept out of Wheeling Traction Company for the express purpose of preventing the lien of the mortgage and its after-acquired property clause attaching to it (R. 19); that the subsidiaries taking title were wholly owned, dominated and controlled instrumentalities of West Penn Electric Company and West Penn Railways Company (R. 14-19).

The complaint further charges that the Board of Directors of the Wheeling Traction Company was wholly ignored in the several transactions which took place merely upon direction of West Penn Electric Company officials (R. 19). Neither the trustee in the mortgage nor the District Court were ever advised of the situation. The trustee was made a party and answered that it had no knowledge of the above facts (R. 52).

The Cooperative Transit Company discovered the facts shortly before the title was transferred to the two last named holders.

The relief asked was: that the several conveyances of title be declared void; that title be conveyed to the purchaser, Cooperative Transit Company; for a discovery and accounting of rents from the West Penn corporations; that Centre Foundry & Machine Company be prohibited from interfering with plaintiff's possession of the car barn; and for General Relief (R. 33, 34).

Motions to dismiss for lack of jurisdiction were made by all the West Penn System corporations and by the Foundry Company and Narrigan on the ground of lack of ancillary jurisdiction (R. 54, 55).

Rulings of the Court Below.

The District Court dismissed the complaint for lack of ancillary and supplemental jurisdiction (R. 57 et seq.) and entered judgment of dismissal accordingly (R. 63).

The Circuit Court of Appeals affirmed the judgment of the District Court and entered an order for dismissal accordingly (R. 73).

The reasons of both courts for dismissal were the same.

First, this proceeding brings in new parties who are necessary if not indispensable to a complete settlement of the controversy.

Second, the specific parcel of realty, the car barn property, was not and could not have been before the court in the prior action.

Third, the issues in the instant proceeding are entirely new; the title and interest of the purchaser and the two defendants holding title could not have been adjudicated in the foreclosure suit.

Fourth, the equities do not favor the purchaser.

It further held:

> "In affirming the judgment below, we are holding simply that the District Court lacks jurisdiction of the instant proceeding on the ground that it is an ancillary proceeding. We do not, in any way, intend to preclude further inquiry into the affairs of the Wheeling Transit Company and its relations with holding companies and subsidiary companies, particularly with reference to the car barn property, if all of the necessary parties are brought in, and a suitable legal basis for such an investigation can be found" (R. 73).

Specifications of Errors to be Urged.

The Circuit Court erred:

1. In holding that the specific car barn property was not and under the circumstances could not have been before the District Court in the winding-up and original foreclosure suit, when the mortgagor, the trustee in the mortgage, the corporations perpetrating the fraud and the subsidiary corporation to whom title was transferred were then present before the court.

2. In holding that the Foundry Company and Narrigan, the holders of a deed for the car barn property with notice, and whose purchase money was placed in escrow upon their insistence, awaiting determination of title were new parties

whose presence in the second suit defeated ancillary and supplemental jurisdiction.

3. In holding that the issues in the second suit were entirely new.

4. In holding, in effect, that the jurisdiction of the District Court was exhausted and a new suit was required to recover assets of a mortgagor or the proceeds thereof, fraudulently concealed in the original foreclosure suit.

5. In holding in effect that alternative relief could not be given—that is to say, that the Foundry Company and Narrigan could not be dropped as parties and the cause proceed against those guilty of the fraudulent withholding who were parties to both suits.

6. In holding, in effect, that there is no inherent ancillary and supplementary jurisdiction in a second suit to correct fraud in a prior suit in a Federal Court.

7. In denying a purchaser at a Federal Judicial sale its rights as a party.

Reasons for Granting the Writ.

1. The Circuit Court of Appeals in denying ancillary and supplemental jurisdiction because of the presence of new parties—the present holders of title with notice (the Foundry Company and Narrigan)—is in probable conflict with the decisions of this court. *Independent Coal & Coke Company* v. *U. S.* (1927) 274 U. S. 640, holding that the presence of a subsequent holder of title with notice of a fraud and not a party to the prior action did not defeat ancillary jurisdiction of a second suit to correct the fraud. *Freeman* v. *Howe, et al.* (1861) 24 How. 450, holding that ancillary or supplemental jurisdiction is not confined to the original parties to the prior suit; also *Pacific R. R. of Mo.*

v. *Mo. Pacific R. Co.* (1884) 111 U. S. 505; *Central Union Trust Co.* v. *Anderson County, Tex.* (1925) 268 U. S. 93. And in probable conflict also with the decision of the Circuit Court of Appeals, Eighth Circuit, in *Ferguson et al.* v. *Omaha & S. W. R. Co. et al.* (1915) 227 Fed. 513, holding that persons not parties to the original foreclosure suit who acquired some interest in the property covered by the mortgage pending the suit and who asserted rights thereto after foreclosure decree and sale, are proper parties to an ancillary suit by the purchaser.

2. The Circuit Court of Appeals in denying jurisdiction on the ground that the specific parcel of realty—the car barn—was not and could not have been before the court in the prior foreclosure action, is in probable conflict with the decision of this Court in *Wade* v. *Chicago S. & St. L. R. Co.* (1892) 149 U. S. 327, holding in a foreclosure suit that the after-acquired property clause of a mortgage brings to it all legal and equitable interests of the mortgagor; and the lien of the mortgage is superior to the title of a third person holding title; and in probable conflict with the decision of the Circuit Court of Appeals for the Third Circuit in *Guaranty Trust Company* v. *Atlantic Coast Electric R. Co.* (1905) 138 Fed. 517, holding that a third person holding title to after-acquired property could be compelled to restore the property or proceeds in the original foreclosure suit; in probable conflict also with the decision of this court in *McGourkey* v. *Toledo & O. C. R. Co.* (1892) 146 U. S. 536, in which it was held that under a mortgage with an after-acquired property clause a foreclosing court could require a third person holding title to deliver up property of the mortgagor.

3. The Circuit Court of Appeals in denying ancillary and supplemental jurisdiction on the ground that the issues in the instant proceeding are entirely new, that the title and

interests of the purchaser and the defendants holding title could not have been adjudicated in the original foreclosure suit, is in probable conflict with the decision of this court in *Independent Coal & Coke Co.* v. *U. S.* (*supra*), holding that a party whose interest arises subsequent to the prior action can be brought in by a supplemental bill unless it was a bona fide purchaser for value, as well as in *Alexander* v. *Hillman* (1935) 296 U. S. 222, in which assets of a corporation being wound up (extravagant salaries to officers in control) were reached by ancillary and supplemental proceedings.

4. The Circuit Court of Appeals in denying ancillary jurisdiction is in probable conflict with Rule 21 of the New Federal Rules providing that parties may be dropped or added on motion or by the court of its own initiative at any stage of the proceeding.

5. The Circuit Court of Appeals is in probable conflict with the decision of this court in *Blossom* v. *Milwaukee & Chicago R. R. Co.* (1863) 1 Wall. 655-658, which holds that a purchaser subjects himself *quoad hoc* to the jurisdiction of the court; and acquires rights in regard to the subject matter of the litigation which the court is bound to protect.

Conclusion.

For the reasons stated, the writ should issue herein as prayed.

COOPERATIVE TRANSIT COMPANY,
By H. B. MCCUNE.

February, 1943.

STATE OF WEST VIRGINIA,
County of Ohio, ss:

H. B. McCune, being duly sworn, deposes and says that he is the president for the petitioner in the above-entitled

matter; that the foregoing petition is true to his own knowledge except as to the matters as therein stated to be alleged on information or belief and that as to those matters, he believes it to be true.

H. B. McCune.

Sworn to before me this 20th day of February, 1943.

Thos. J. Garden,
Notary Public, Ohio County.

[seal.]

My commission expires Jan. 15, 1944.

Jay T. McCamic,
Counsel for Petitioner,
The National Bank of
West Virginia Bldg.,
Wheeling, West Virginia.

Of Counsel:
Jay T. McCamic.

PETITIONER'S BRIEF

SUPREME COURT OF THE UNITED STATES

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COOPERATIVE TRANSIT COMPANY,
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WEST PENN ELECTRIC COMPANY, A CORPORATION, WEST PENN RAILWAYS COMPANY, A CORPORATION, TRI-STATE IMPROVEMENT COMPANY, A CORPORATION, WEST PENN SYSTEM CONSTRUCTION COMPANY, A CORPORATION, WEST PENN SECURITIES DEPARTMENT, INC., A CORPORATION, CENTRE FOUNDRY & MACHINE COMPANY, A CORPORATION, CLARA NARRIGAN.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

Opinions.

One opinion was delivered by the District Court. It was written by District Judge William E. Baker and filed the 5th day of August, 1942 and appears on page 57 of the record and is reported in 46 Fed. Supp. 59.

The opinion of the Circuit Court of Appeals (Circuit Judges Baker, Dobie and Coleman, District Judge; Judge Dobie writing) was filed January 2, 1943 and appears at page 66 of the record. It is not yet reported.

Jurisdiction.

Jurisdiction is based upon Judicial Code, Section 240(a) as amended, by Act of February 13, 1925 (28 U. S. C. A. Section 347(a)).

In view of the union of petition and brief a re-statement of questions presented and of the specifications of errors to be urged is omitted and not presented a second time.

The Facts.

The essential facts are set out in the statement in the petition (p. 5) and are not repeated here. We emphasize, however, the situation. Title to real property belonging to a mortgagor is secretly withheld for the express purpose of preventing the lien of the mortgage attaching and conveyed to a subsidiary in a unity of corporations owned and dominated, by a central source, of which the mortgagor was a part. The title subsequently passed from one of the corporations to another in the unity and finally left the unity to the present holders of title who took with notice and whose purchase money is now in escrow. A prior action of winding-up the mortgagor and foreclosure was had in a District Court (to whom no disclosure of the above facts was made) which by its decrees found the mortgage a lien upon all the property of the mortgagor, both legal and equitable. The District Court conveyed to the purchaser all the property of the mortgagor subject to the mortgage, free and clear of all claims including equity of redemption. The trustee in the mortgage, the dominant corporations in the unity or

system and the corporation holding title were parties to the prior action. In the present ancillary and supplemental action the only new parties are the present holders of title, who are in privity with the old parties to the prior action through notice, and two of the subsidiary corporations in the unity.

Argument.

The first suit was a winding-up of an insolvent corporation and a foreclosure of its mortgage. The District Court took jurisdiction. Legal title to part of the property covered by the mortgage had been conveyed fraudulently to one of the parties, though the court was unaware of this when it found the mortgage a subsisting lien upon all the property of the mortgagor and caused the same to be sold to a purchaser.

The second suit is by the purchaser to recover the assets, for discovery and for general relief. All parties to the first suit are joined and additional parties who the complaint alleges took with notice.

I.

The decision of the Circuit Court of Appeals conflicts with the decisions of this court and the courts of other Circuits, holding that there is ancillary or supplemental jurisdiction of a second suit to correct fraud or to further deal with property in custody or control of the court in the first suit. The presence of new parties is no bar if there is privity to parties in first suit: even strangers are proper parties if their interest concerns property in the custody or control of the court in the original suit.

In *Independent Coal & Coke Co.* v. *United States* (1927), 274 U. S. 640, the first suit was brought to restore lands to the government, title to which had been obtained through

fraud. A decree was obtained. The State of Utah which had the legal title, and was not a party to the first suit (the U. S. having only equitable title), conveyed the legal title to the Carbon County Land Company, created and controlled by those originally guilty of fraud.

The second suit was in the nature of a supplemental bill in aid of the former decree. The Carbon County Land Company and the Independent Coal & Coke Company were made parties defendant. The objection was made that the Independent Coal & Coke Company was not a party to the fraud and that it had not acquired any interest from or under any other party to the transaction.

It was held that unless the Coal & Coke Company was a bona fide purchaser—matter of defense—it was a proper party, taking title subject to the equities of the United States and a constructive trustee, it appearing that its interest was acquired subsequent to the transfer of title by the Government to the State of Utah.

This court further held that the United States could follow the property until it reached the hands of an innocent purchaser for value; that one who fraudulently procures a conveyance may not defeat the defrauded grantor or protect himself from the consequences of his fraud by having title conveyed to an innocent third person; that the fraud persists in every interest acquired and in the proceeds which the government could reach.

On the question of new parties, p. 649.

> "But it is argued that there are no allegations showing that petitioner, Independent Coal & Coke Company, is a party to the fraud or what interest it claims in the lands, or that it acquired any interest from or under any other party to the transaction. But we think it fairly inferable from the bill, taken as a whole, that the interest alleged to be claimed by the coal company was

one arising subsequent to the conveyance by the state to the Land Company. The bill sets up title in the United States and its transfer to the state alleging that the state of Utah in making the transfer relied on the fact that it had not parted with the legal title to the lands at the time of the decree. This in effect is an averment that the interest claimed by the coal company was acquired subsequent to the certification by the United States to the state. Whatever interest it acquired after that event, it took subject to the equities of the United States, and if from the land company, subject also to all of the equities against that company, unless the purchase price was bona fide. Bona fide purchase is an affirmative defense. *Wright-Blodgett Co.* v. *United States,* 236 U. S. 397, 403, 35 S. Ct. 339, 59 L. Ed. 637."

(*Wright-Blodgett* v. *U. S., supra,* decided that the burden is on the grantee to establish that he is a bona fide purchaser.)

It is important to note that since the bill had not been well drafted, leave was given to perfect it.

The close analogy to the case at bar is clear; in both there is fraud; in the case cited the fraud was established by the first suit; in the case at bar the fraud is pleaded as fraud upon both the mortgagor, the trustee, and the District Court, a fact that must be accepted on a motion to dismiss; in both there is objection that a new party is joined—a bona fide purchaser; in the case cited this court said that was a matter of defense; the Circuit Court of Appeals in the case at bar held the Foundry and Narrigan were new parties, although their interests were acquired with notice and the purchase money placed in escrow.

Alexander v. *Hillman* (1935) 296 U. S. 222, started as a winding-up with a receivership; thus the subject matter of the main suit was the collection and distribution of assets of the business being wound up—the identical purpose of

the prior suit of the cause at bar which had the added feature of a mortgage foreclosure.

The purpose of the ancillary bill in *Alexander* v. *Hillman* was to collect assets not reached in the prior suit—namely large sums paid under the guise of salaries to officers. These officers—defendants to the second suit—had filed claims in the first. The bill was dismissed for want of jurisdiction and the Circuit Court of Appeals, Fourth, sustained the lack of jurisdiction. This court reversed, holding that the defendants were parties to the first suit through the filing of claims and no process need be served upon them.

The Tri-State Improvement Company, a party to the first suit, originally took dry little "as intermediary" for the Traction Company and it filed a claim in the first suit. The second suit here was to reach an asset owned by the mortgagor coming under the jurisdiction of the court in the first suit. *The District Court had jurisdiction of the equity of the mortgagor and control of the party holding dry title.*

The Circuit Court of Appeals in the case at bar held that the specific property—the car barn—was not before the court in the first suit. The equitable interest of the mortgagor, however, was always present. In *Wade* v. *Chicago S. & St. L. R. Co.* (1892), 149 U. S. 327, this court held that an after-acquired property clause brought the equitable interests of the mortgagor to the mortgage notwithstanding the conveyance of legal title. Only the dry legal title was in a party to the first suit—the Tri-State Improvement Company. The conflict with *Alexander* v. *Hillman* and *Wade* v. *Chicago S. & St. L. R. Co.* holdings is apparent.

In the 3rd Circuit *Guaranty Trust Company* v. *Atlantic Coast Electric R. Co.* (1905), 138 Fed. 517, there was a foreclosure of a mortgage with an after-acquired property

clause. Title to property bought and paid for by the mortgagor was in a controlled corporation and the beneficial interest in the mortgagor. Equitable ownership of the property was determined to be in the mortgagor and the outstanding interest in the controlled corporation was called in.

In the case at bar, the District Court had decreed the mortgage a lien upon all of the property and assets of the Traction Company, both in law and in equity. The subsidiary corporation holding title was a party. The District Court had complete jurisdiction to compel the transfer of legal title. The holding of the Circuit Court of Appeals that the specific property was not before the District Court in the first suit or in other words, that the District Court could have done nothing, is in conflict with the above cases.

The District Court had before it in the original suit every party to the fraud. The equitable interest of the Traction mortgagor was subject to the lien of the mortgage and hence within the control of the court; the title was in one of the corporate subsidiaries then present in court as a party.

The Court could have granted complete relief as shown by the above cases in the first suit. The essential conflict is this: the Circuit Court of Appeals has held in the case at bar in effect that conveyance of legal title to mortgaged property to a third person prevents a foreclosing court from calling in legal title from the third person present as a party before it, for the court said (R. 72):

> "The specific parcel of realty, the car barn property, was not (and under the circumstances could not well have been) before the court in the prior action."

This is in direct conflict with *Gauranty Trust Company* v. *Atlantic Coast Electric R. Co., supra,* and *Wade* v. *Chicago S. & St. L. R. Co., supra.*

II.

The Conflict in Reference to New Parties.

Independent Coal & Coke Co. v. *U. S., supra,* brought in a new party in the second suit. It claimed that it had not bought from any party to the preceding suit and consequently was innocent. The court held (as seen by the quotation, pp. 18-19 ante) that it was inferable that it had bought subject to equities unless it was a bona fide purchaser which was an affirmative defense. This was a matter, therefore, that went to the merits, not to jurisdiction.

In this case there are no strangers; the so-called new parties are in privity with the parties to the former suit.

The corporations originally diverting title and the one taking title were parties to the original suit; active fraud was charged against them.

The subsequent history of the title shows that it passed to other corporations in the unity of corporations making up the West Penn System, with complete stock ownership, control and interlocking directorates.

The immediate holders of title, the Foundry Company and Narrigan, took title with notice and required the purchase money to be put in escrow until title could be determined (p. 27 complaint, R. 29). The transaction is not yet completed. Under *Grogg* v. *Stevens* (1925), 6 F. (2d) 862 (C. C. A. 4th) following general law, one is not a bona fide purchaser who pays the consideration or part of it after notice. Unless privity is broken the proper parties and the same property withheld in the prior suit are still before the court.

The fact that parties are "new" is never a bar to the second suit. The test is: are they in privity to parties in the

prior suit or does their interest concern property or the subject matter within the custody or control of the court in the prior suit?

Freeman v. *Howe, et al.* (1861), 24 How. 450;
Pacific R. R. Co. of Mo. v. *Mo. Pacific R. R. Co.* (1884), 111 U. S. 505.

In *Central Union Trust Co.* v. *Anderson County, Tex.* (1925), 268 U. S. 93, the court said, p. 96:

> "Ancillary suits are not limited to those initiated by persons who desire to come in and have their rights determined. Such a suit may be maintained by the plaintiff in the principal suit against strangers to the record to determine a controversy having relation to the property in the custody of the court and which in justice to the parties before the court, ought to be determined in the principal suit."

There was a reservation in the decree of sale in a railroad mortgage foreclosure permitting repossession upon failure of the purchaser to fulfill the contract of sale and reserving questions relating to the property. The District Court was held to have jurisdiction subsequent to the decree confirming sale at the suit of the purchaser to prohibit enforcement of a judgment of a State Court requiring burdensome maintenance of general offices, shops, etc. in a particular locality.

In the case at bar the court in purchaser's deed reserved the right to retake the property for default in payment of purchase price and gave the purchaser a covenant of further assurance as to "the property herein described, referred to and/or intended herein to be granted, conveyed • • • with appurtenances • • •" (R. 50).

III.

The District Court, not yet having given complete relief, has not yet exhausted its jurisdiction as to the Equitable interest of the Traction Company in the car barn property. This second suit is to further deal with the subject matter of the original foreclosure.

Wade v. *Chicago S. & St. L. R. Co.* (1892), 149 U. S. 327, is the leading case for the proposition that an after-acquired property clause brings to the mortgagee the equitable rights of the mortgagor notwithstanding the fact that actual title to the property has been conveyed to other persons.

The exact language of the court, p. 341:

> "* * * the 'after-acquired property clause' of a mortgage will cover not only legal acquisitions, but all equitable rights and interests subsequently acquired *by or for* the mortgagor." Citing among others the case of *Central Trust Co.* v. *Kneeland* (1890), 138 U. S. 414. (Italics ours.)

In the Wade case the title had been conveyed to a third person and was not in the mortgagor.

It seems apparent that the District Court (in the case at bar) in the first suit had complete jurisdiction of the equitable interests of the Traction Company mortgagor.

In *McGourkey* v. *Toledo & O. C. R. Co.* (1892) 146 U. S. 536, there was an after-acquired property clause and title to rolling stock was in a third person. The court said, p. 553:

> "* * * We know of no rule of law which will estop the mortgagee *or a purchaser* at a foreclosure sale from insisting that the railway thereby acquired the title to the property, and that it had become subject to the lien of the mortgage * * *". (Italics ours.)

These two cases are cited to show the extent of the jurisdiction of the District Court in the first suit of winding-up and foreclosure when property of the mortgagor has been conveyed to a third person.

It is apparent that the District Court attempted to dispose of all of the property of the Traction Company. The language of foreclosure decree finds the mortgage a subsisting lien upon all of the property in law or in equity of the Traction Company (R. 7). The decree of sale directs that property to be sold. The decree confirming sale uses the same language. The deed to the purchaser which has a covenant of further assurances conveys specifically what was authorized to be sold.

The difficulty here is that the District Court did not know of the interest of the mortgagor in the car barn property—through fraudulent concealment of parties to the original foreclosure who are parties here who now move to dismiss.

If the general language of the court operated upon the interest of the mortgagor in the car barn property (a matter which involves construction of the decrees of the court) then the interest is now in the purchaser, the petitioner here, which submits itself to the court. If, on the other hand, it did not operate upon this interest of the mortgagor it is yet undisposed of; upon appointment of the Receiver the constructive, if not actual possession of the equitable interest (or the legal interest if the trust in the Tri-State were merely passive) came to the court and is still there. Otherwise undiscovered fraud terminates the jurisdiction of the court, which is an abhorrent doctrine and violating the fundamental jurisdiction of a court of equity to correct fraud.

If, finally, the decrees of the District Court had no effect at all, then the interest is still in the trustee in the mortgage (who is a party here) and is property against which the lien

of the mortgage is unforeclosed and the District Court has not yet exhausted its jurisdiction.

> "The jurisdiction of a court is not exhausted by the rendition of its judgment, but continues until that judgment shall be satisfied." Chief Justice Marshall in *Wayman* v. *Southard* (1825) 10 Wheat. 1, p. 23.

In *Alexander* v. *Hillman, supra,* the *res* in the first suit which was reached in the second suit was a claim for overpaid salaries.

The *res,* the estate of the mortgagor, in the car barn property was an equitable estate which was always there. The fraudulent withholding of it was the cause of action. The subsequent discovery merely uncovered the cause of action but did not create it. In this it differed from *International-Great Northern Ry. Co.* v. *Binford,* 10 Fed. (2d) 496, cert. den. 273 U. S. 694, where the cause of action *arose subsequent* to the prior suit. It differs also from *New Orleans Land Co.* v. *Leader Realty Co.* (1921) 255 U. S. 266, where land was sold by a receiver duly appointed by a federal court in satisfaction of a judgment recovered in a prior suit and the claimant of a superior title thereafter obtains a favorable judgment in a state court. A suit in the Federal Court to restrain the enforcement of the State Court judgment was not ancillary to the former suit, as the action of the State Court did not interfere with anything done in the National Court, and the relief sought was not necessary to protect or render the former decree effective. While here, the winding-up and foreclosure was *in rem*; the equity of the Traction Company was before the court in the first suit as well as the legal title through the presence of the subsidiary fraudulently holding the dry legal title who is also now a party. All parties necessary to bring the complete title in were before the court in the first suit. The distinctions, in these cases, we submit, are clear.

Brun v. *Mann* (1906) 151 Fed. 145 (C. C. A. 8th) is an authority on the scope of ancillary jurisdiction. Mann had recovered a judgment against Tillett in 1885 in a Federal Court. Mann sought to satisfy his judgment against the estate of Tillett by an ancillary proceeding about 15 years later (following an action which Tillett's administratrix lost, to have the judgment cancelled, in which suit Mann's judgment was revived).

Objection to jurisdiction was made. The court held, Judge Sanborn writing, that it was a dependent suit.

> "Such dependent suit is but a continuation in a court of equity of the original suit to the end that more complete justice may be done."

It listed also the grounds of ancillary and supplemental jurisdiction:

> "(1) to aid, enjoin, or regulate the original suit;
>
> (2) to restrain, avoid, explain or enforce the judgment or decree therein; or
>
> (3) to enforce or obtain an adjudication of liens upon, or claims to property in the custody of the court in the original suit."

The Circuit Court of Appeals in the instant case narrows the scope of dependent jurisdiction.

> "(1) proceedings which are concerned with the pleadings, processes, records or judgments of the court in the principal case;
>
> (2) proceedings which affect property already in the custody or control of the court" (R. 70). (Citing Dobie on Federal Procedure, §84, page 322).

We submit that the holding of the Circuit Court of Appeals is in conflict with the law governing ancillary jurisdiction which covers the case where complete relief has not

been administered in the first suit, and especially where fraud of parties to the first suit prevented the court's doing so.

IV.

The holding of the Circuit Court of Appeals is in conflict with the law (now Rule 21 New Federal Rules) which permits the dropping or adding of parties on motion or by the court of its own initiative at any stage of the action.

Objection can hardly be made that the petitioner took no action, for no opportunity for amendment was provided. The District Court in fact said the complaint could not be amended (R. 62).

The bill not only asked for a discovery and accounting, but for general relief as well.

If the Foundry Company and Narrigan are not proper parties and if the specific car barn property was not before the Court in the original suit, there remain as parties, the trustee in the mortgage; the corporations who were members of the unity of corporations dominated and controlled by the corporations committing the fraud, all except two (who are, however, owned and controlled corporations as the others) were parties to the prior suit.

The specific property was conveyed away by act of parties to the first suit who are also parties to the second suit. There remain, therefore, the proceeds of the car barn property which equity can follow and reach, and all necessary parties are before the court.

Why does not jurisdiction exist as to these without the presence of the Foundry Company and Narrigan?

This point on jurisdiction is emphasized because the Circuit Court of Appeals recognized that the District Court had not yet exhausted its jurisdiction. It expressly restricted its holding on the ground that the presence of the

Foundry Company and Narrigan and that the specific car barn property was not before the Court in the prior suit, defeated ancillary or supplemental jurisdiction in the same court. It said it did not preclude further inquiry into the affairs of the Wheeling Traction Company and its relation with holding companies and subsidiary companies, particularly with reference to the car barn property "if all of the necessary parties are brought in, and a suitable legal basis for such an investigation can be found" (R. 73).

The "Deeprock Doctrine" is pertinent. *Taylor* v. *Standard Gas & Electric Co.* (1939) 306 U. S. 307.

This seems to concede the dependent and not yet exhausted jurisdiction obtained in the first suit which is exemplified in the cases cited, as the historic subject of ancillary and supplemental jurisdiction.

Furthermore it seems a cause for the proper employment of the authority of rule 21 above referred to.

To require an original suit to be brought in a different court to satisfy the requirements of diversity of citizenship to correct the necessarily conceded fraud in the prior suit, in effect emasculates the remedy. Dependent jurisdiction was created to prevent this.

V.

The Circuit Court of Appeals did not recognize the rule that ancillary and supplementary jurisdiction in a second suit to correct fraud or abuse in a prior suit is inherent in a Federal Court.

From the earliest times the Federal Courts have exercised inherent jurisdiction to prevent abuse, oppression and injustice. A leading case is *Krippendorf* v. *Hyde* (1884), 110 U. S. 276.

Pacific R. R. of Mo. v. *Mo. Pacific R. Co.* (1884), 111 U. S. 505 was the case of a mortgage foreclosure in which a sale

was had and affirmed in this Court. Thereafter an ancillary and supplementary proceeding was begun alleging fraud in fact in the foreclosure suit, in the conduct of the lawyer and directors of the corporate mortgagor, and praying that the decree of foreclosure be set aside. *New parties were made.*

Jurisdiction was sustained on the ground that the charges of fraud alone warranted discovery and the relief sought.

In the case of *Ferguson* v. *Omaha etc. R. Co.* (1915), 227 Fed 513 (C. C. A. 8th), there was a mortgagor foreclosure pending which the mortgagor under to convey certain rights in land to third persons, who asserted such rights after foreclosure decree and sale. The right of the purchaser to bring in such third persons to have their rights adjudicated and declared subject to the decree was declared ancillary to the foreclosure.

The Circuit Court of Appeals, 4th, recognized the force of the above cases in the Supreme Court in *Ross* v. *Miller* (1918), 252 Fed. 697, which was an ancillary and supplemental suit to cancel a release of judgment as procured by fraud and to subject an equity in land to payment of the judgment.

VI.

The Circuit Court of Appeals in determining that the equities do not favor the purchaser (petitioner) necessarily construed the decree in the first suit and thereby to that extent invoked the very ancillary jurisdiction which it denies; it invaded the rights of the purchaser in so doing.

The Circuit Court of Appeals observed that it seemed a fair inference that the purchaser received all it intended to acquire and all it paid for under the judicial sale (R. 73).

It is submitted that this has no bearing on jurisdiction except that this determination itself involved the construction of the decrees without a full hearing. The purchaser is a

party to the former suit (*Blossom* v. *Milwaukee & Chicago R. Co., supra*). The purchaser paid a cash consideration; in addition it assumed all the obligations of the Receiver (which extended the jurisdiction of the District Court (*Central Union Trust Co.* v. *Anderson County, Tex., supra*); and it agreed to pay all taxes, which were liens on the property purchased (R. 49, 50). What this amounted to was not pleaded and never before the court. The purchaser fully complied with the terms of its purchase.

The purchaser bought all of the properties of the Traction Company subject to the mortgage which included

> "* * * car houses * * * car shops"
> "* * * all the estate, right, title, interest, property, possessions, claim and demand whatsoever, as well in law as in equity. * * *"
> "It is intended hereby to convey all property of any sort or nature whatsoever, whether real, personal or mixed, which the Traction Company now owns, or which it may hereafter acquire * * *" (R. 4, 5).

The property could not be described as to every item; an *omnium gatherum* to catch all loose ends was therefore necessary. The purchaser could only know that it had bought *all* the property of the Traction Company. The deed to purchaser was free from any right of redemption (R. 49). Furthermore there was a covenant of further assurance (R. 50). The purchaser is the legal owner of any claim which the Traction Company had by the Act of the District Court. Whatever purchaser's equities or those of any one else are, the construction of the decrees in the first suit is irrevocably involved. The purchaser has the right to know what he does not own to the same extent as what he does own under the decrees.

A purchaser from a Federal Court complying with his purchase has a right to a construction of the decree in the court making the sale;

Blossom v. *Milwaukee & Chicago R. R. Co.* (1863), 1 Wall. 655-658.

> "A purchaser or bidder at a Master's Sale in chancery subjects himself *quoad hoc* to the jursidiction of the court, and can be compelled to perform his agreement specifically. It would seem that he must acquire a corresponding right to appear and claim at the hands of the Court, such relief as the rules of equity proceedings entitle him to."

If neither the car barn property nor the proceeds in lieu thereof belong to the purchaser, it is entitled to know if those entitled should not equitably bear a share of the Receiver's contracts and the lien of taxes—which the purchaser has paid. Allowing the ancillary jurisdiction does not endorse the claim of the purchaser but it does present an issue to the court for the necessary and equitable adjudication among those entitled, all of whom were made parties.

The purchaser is an electric street railway whose properties are devoted to public use. It pleaded that the car barn was absolutely necessary and essential to maintenance of service. There is no other available site (R. 32).

In the present emergency it is imperative that service be maintained (R. 32). The purchaser has the valuable right to be a bidder for this property specially built for use as a car barn, if it is put up for sale again, and it has the right to have the decree construed as an issue of law.

The fact cannot be overlooked that the trustee for the bondholders was made a party to the ancillary proceeding and it will upon the merits insist upon the rights of the mortgagee. The trustee did not question jurisdiction, but immediately filed its answer confirming that no disclosure of facts pleaded had been made to it.

In any suit working out the inquiry which the Circuit Court intended to be made, the purchaser is an indispensable

party because the court conveyed to it all of the property, real and personal, subject to the lien of the mortgage, free and clear of any equity of redemption. It is the actual holder of title.

Finally the purchaser bought *caveat emptor;* it took the risk of less or more than appeared; if there was less it could not complain; if there is more in its deed that it should have, it is entitled to a construction and to what extent those to whom the car barn or the proceeds belong, should share in petitioner's discharge of Receiver's obligations and taxes in compliance with the decree of sale and purchase.

Conclusion.

We do not believe the principles enunciated by the Circuit Court of Appeals, 4th, are uniform with those of this Court and those of the courts of other circuits as shown by the cases cited, and, consequently, the law in the Fourth Circuit is uncertain.

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